

# TRANSCRIPT OF PROCEEDINGS

ORIGINAL

UNITED STATES OF AMERICA

DEPARTMENT OF ENERGY

MEETING OF  
THE  
NATIONAL PETROLEUM COUNCIL

Washington, D. C.

Wednesday, October 28, 1987

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1 UNITED STATES OF AMERICA

2 DEPARTMENT OF ENERGY

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4 MEETING OF THE

5 NATIONAL PETROLEUM COUNCIL

6 Dolley Madison Ballroom

7 The Madison Hotel

8 Fifteenth & M Streets, N.W.

9 Washington, D. C.

10  
11 Wednesday, October 28, 1987

12  
13 The meeting of the National Petroleum Council convened  
14 at 9:07 a.m., Edwin L. Cox, Chairman, presiding.  
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## P R O C E E D I N G S

CHAIRMAN COX: Good morning, ladies and gentlemen. Welcome to the meeting of the Petroleum Council. You have an agenda before you. We will try to follow that. We appreciate the excellent turnout we have. You are always wonderful to respond to the meetings, and we are delighted you are here.

Now, if you have no objection, the check-in at the door will serve as the roster count and the attendance check and we will not call the roll at this time.

I did want to point out there is one person missing. Many of you have noticed maybe this morning -- and I know you have over the years -- there was always a familiar face sitting at the front door greeting us as you entered the room. Wylie Whisonant missed only one meeting of this council since it was established in 1946 until he became ill earlier this year. Wylie had been an employee of the Department of the Interior, where he assisted every Secretary of the Interior from 1936 until he retired in 1971.

Following his retirement, he joined the National Petroleum Council staff. He was an inspiration to all. He passed away on March 6 of this year at the age of 84. I am sure he will be missed by all because he was always so nice and friendly and greeted us as we came in.

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1                   Therefore, with sincere appreciation for his  
2 achievements and contribution to the industry and the  
3 council, and with a sense of great loss, be it resolved on  
4 this 28th day of October 1987 that the deepest sympathy of  
5 the members of the National Petroleum Council be extended to  
6 his widow, Virginia, and the family of Wylie Whisonant, that  
7 this be entered upon the permanent record of the council,  
8 and that an appropriate copy be delivered to his family as a  
9 remembrance of the council's esteem and deep appreciation.

10                   Ladies and gentlemen, if you would not mind, I  
11 propose that we signify adoption of this resolution by  
12 rising for a moment in silent reflection and prayer.

13                   (Pause.)

14                   CHAIRMAN COX: Thank you very much.

15                   You all know the people at the head table. But I  
16 would like to introduce, on my left, Lod Cook, vice chairman  
17 of the council. Next to Lod is J. Allen Wampler, assistant  
18 secretary for fossil energy. At my far right, Marshall W.  
19 Nichols, executive director of the council. Next to  
20 Marshall is Bill Swales, chairman of the NPC committee on  
21 petroleum storage and transportation.

22                   On my immediate right, as we all know, is the  
23 Honorable John S. Herrington.

24                   We are very pleased, Mr. Secretary, that you  
25 could join us this morning for our first item of business.

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1 We are always delighted to hear from you.

2 I am also pleased to announce that the Secretary  
3 has agreed to answer any questions and comments after his  
4 remarks. So we will open it for questions at that time.

5 It is a pleasure, Mr. Secretary, to introduce you  
6 at this time.

7 SECRETARY HERRINGTON: Thank you.

8 (Applause.)

9 SECRETARY HERRINGTON: Thanks, Ed. This is a  
10 little different atmosphere than there was last year at this  
11 same time, I think most of you will agree. I remember Bobby  
12 Parker was hunting down at his ranch, deer hunting -- I  
13 forget who he was with, one of the guys in this room. They  
14 had shot a deer, and they were dragging it out to the truck.  
15 They had the truck pretty far out in the brush there, and  
16 they dragged it by the hind feet and they were pulling it  
17 toward the truck and the antlers were catching in the ground  
18 and catching in the brush and hooking in the trees as they  
19 were going out.

20 And they were working up a sweat. This was a  
21 heavy deer. They were really getting a little tired, and  
22 they met one of the ranch hands there on the way out. He  
23 said, "Mr. Parker, I think it would go easier if you would  
24 drag this deer by the antlers," and he said, "then you  
25 wouldn't be digging in the dirt and hooking the brush."

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1 So he -- and I forget, it might have been Ray,  
2 I'm not sure.

3 (Laughter.)

4 SECRETARY HERRINGTON: They walked around and  
5 grabbed the deer by the antlers and started pulling it.  
6 They went a little distance. They looked at each other and  
7 said, "Yes, this is much better. We're not getting any  
8 problems here. But Bob said, "You know, there's only one  
9 thing that bothers me about this." Ray said, "What?" And  
10 he said, "Well, we're getting farther and farther from the  
11 car."

12 (Laughter.)

13 SECRETARY HERRINGTON: Isn't that true story?

14 (Laughter.)

15 SECRETARY HERRINGTON: I think, you know, we're  
16 still pulling the deer. We're still pulling the deer.  
17 We're pulling in the right way now. We haven't quite  
18 reached the car. Policies are changing. Things are looking  
19 at little better. We have got a long way to go, still.

20 I think there has been a lot of energy debate in  
21 the country, in the Congress, in the industry. Certainly,  
22 we have everybody's attention. I brought an example of  
23 that, the energy security study. The President has now  
24 reached fame and fortune. It has been now been translated  
25 into Japanese, and they have sold more copies than we have.

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1 We are on our third printing, 20,000; and I think they are  
2 substantially over that. So this is obviously the sign of  
3 success.

4 I wanted to talk about a couple of things this  
5 morning and the maybe take some comments and questions that  
6 you would be interested in.

7 Obviously, the number one issue on everybody's  
8 lips today is the economy: What has been going on? How  
9 does that affect what we have been doing, our policies?  
10 What does it mean for oil import tax; is that back on the  
11 table? How are we going to deal with all of this?

12 I have just returned from a visit to eight  
13 countries in the Gulf. I thought I would talk about that a  
14 little bit. We spent about two weeks over there. We met  
15 with the leader of every country, every energy minister,  
16 every finance minister, every prime minister. We went from  
17 Turkey to Kuwait to UAE to Bahrain to Qatar, Saudi Arabia,  
18 Morocco, and obviously, Egypt.

19 The number one issue obviously is the Gulf from  
20 top to bottom over there: what is happening, what is going  
21 to happen, how do we see it. The question that I think was  
22 most often asked was does the United States mean it? Are we  
23 there for keeps?

24 There is a great deal of skepticism on the part  
25 of every foreign leader over there. Our record, of course,

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1 following through with commitments with the Shah of Iran and  
2 other incidents is not the best. We have a democracy, and  
3 we tend to change policies in the middle of the stream  
4 sometimes.

5 And we have a number of countries over there that  
6 are operating with what I would like to call a gun held to  
7 their head. They are sitting very close to a belligerent  
8 nation with 40 to 50 million people that basically, from my  
9 impression of what was said by most of the leaders over  
10 there, there is very little coordination of policy in the  
11 government of Iran. There is very little authority of  
12 government officials. People are not authorized to say  
13 certain things. Very few issues go to the Ayatollah, and  
14 there is general disorganization within the hierarchy of  
15 that country.

16 Almost every moderate country in the Gulf has  
17 attempted to reach out to Iran to try to be a middleman or  
18 negotiate peace, without results. Certainly, the U.S. has  
19 used every contact that we know possible through the State  
20 Department, Defense Department, National Security Council,  
21 and we have not been able to begin the kind of talk that  
22 needs to happen.

23 The best hope, and I think the desire of most  
24 countries, would be to have a negotiated peace settlement  
25 through Resolution 598 in the U.N., and then a follow-on



P Wpv 1 resolution of arms embargo. That would be, I think, the  
2 most desirous solution to it.

3 In the interim, you have noticed that the  
4 President has signed an oil embargo against Iran. Actually,  
5 it is more than just an oil embargo. It has hit stronger  
6 than that. It has hit some of the other products that we  
7 are purchasing and exporting to them.

8 We also have some initiatives underway to link  
9 the sale of Silkworm missiles from China with some high-tech  
10 equipment that they have been purchasing from us.

11 So we are making every effort to settle this  
12 before it gets out of control.

13 The President's reasons for the oil embargo, I  
14 think, are several. They have been pretty clear. The  
15 first, I guess the most important one, is the unprovoked  
16 attacks on the merchant vessels that are working in the  
17 international waters. That is a situation that is  
18 intolerable for the United States.

19 The second reason that he has talked about is a  
20 refusal to implement this U.N. Security Council Resolution  
21 598.

22 The third, continued aggression against  
23 nonbelligerent nations in the Gulf.

24 The fourth, what we know today to be a  
25 sponsorship of terrorism from that country elsewhere in the

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1 world outside of the Gulf. It really is a sad scenario that  
2 is taking place.

3 Where are we? 1986, we purchased \$600 million --  
4 \$500 million worth of petroleum -- from Iran in the U.S.,  
5 and \$100 million worth of other products. In the first  
6 months of 1987, January to July, we purchased over \$1  
7 billion from them.

8 The question comes up many times in my  
9 discussions: First of all, is the embargo effective? We  
10 have all lived through embargoes now. We watched the  
11 attempts with the Olympic boycott, which didn't work too  
12 well. The grain embargo, we didn't get anywhere with that.

13 The South African sanctions, I think, have been a  
14 dismal failure. They have not accomplished, and we knew  
15 they did not. All they have done is create some  
16 millionaires in South Africa who have purchased distress  
17 sales and lost a lot of jobs, and I think it jeopardized our  
18 foreign policy in that area.

19 Embargoes are tough. Economically, they don't  
20 make sense. They are hard to administer.

21 That said, I don't think we can afford as a  
22 country not to take the step to prevent this amount of money  
23 flowing into a government that will purchase arms to be used  
24 against our men and women in the Service. So we must take  
25 that step.

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1           The Senate voted 98-0 in favor of an embargo.  
2   The House, I think, was almost unanimous, five votes against  
3   it. And the President feels strongly on it.

4           That said, and since we are now embarked on that  
5   particular course, the success of an embargo will depend on  
6   how we approach it as an industry. For international  
7   companies it will depend on what kind of cooperation we get  
8   from our allies. If we cannot get cooperation from  
9   countries like Japan, West Germany, Italy, other large  
10   purchasers of oil in this market, then it will not be  
11   successful.

12           For that reason, the Japanese -- especially the  
13   Japanese -- must do their part in this embargo to get the  
14   war wound down. We averaged in 1986 90,000 barrels a day of  
15   oil from Iran to the U.S. and to our territories, 250,000  
16   barrels a day in the first seven months of 1987. Then  
17   during July -- I think you read the figures in the paper --  
18   620,000 barrels a day.

19           We have begun to wind that down, and in August of  
20   1987 we estimate about 468,000 barrels a day in August. And  
21   then we are down to, in September, our estimates are 345,000  
22   barrels a day. That is a substantial amount of oil.

23           That said, we area still only getting between  
24   there and five percent of American oil out of the Gulf from  
25   imports, which is not a large amount. The Japanese are

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1 still pulling on the average of about, I would say, a third  
2 of the oil out of the Gulf. It is costly for us to convoy  
3 in the Gulf. We are risking American Service personnel.  
4 The figures are large on our expense of patrolling the Gulf.  
5 The Japanese have so far put together \$10 million in  
6 navigational systems. They have granted some loans to some  
7 of the Gulf countries, and they have been supportive in the  
8 U.N. I think we can expect and we must expect them to do  
9 more.

10 That is a subject that we can talk about in a  
11 minute if you care to. It is certainly one that is on our  
12 number one list.

13 It is obvious to me after talking to oil  
14 ministers -- I spent two hours with King Fahd, time with his  
15 Saud, and it is pretty obvious that they are going to try  
16 very hard to support a price of \$18 in the Gulf regardless  
17 of circumstances. They are committed to it. It will be  
18 difficult at the December meeting that they are having in  
19 Europe. But it looks to me like they are set on the policy,  
20 for those of you who are interested in price.

21 In the meantime, it is interesting to note -- and  
22 I think most of you follow this -- but in the recent events  
23 in the stock market we have not seen the price of oil move  
24 too much this last week. The biggest fluctuation was about  
25 40 cents that I saw. I have been asked over and over again

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1 are the events in the Gulf contributing to the stock market  
2 dislocation in the United States. My answer is that I don't  
3 think they are. Maybe in the short term maybe they have.  
4 Maybe they have a cumulative effect a little bit, a little  
5 bit working in there, but on a short-term basis only.

6 I think investment decisions can depend on a lot  
7 of things. But I find it difficult to believe that events  
8 in the Gulf have been one of the major driving forces.

9 I was reading up to 90 days ago in investor  
10 magazines like Russell and Dow Theory that we are into a  
11 bull market -- I am sorry, a bear market and that the change  
12 had taken place. And I think investment decisions were made  
13 far beyond some of the events that took place in the Gulf.  
14 A number of you are active in the market and may have  
15 different ideas. That is the way I see it from where I sit.

16 We have an interesting situation now. The  
17 President, the administration, the Congress are getting  
18 together to attempt to negotiate some changes in deficits,  
19 which I think will be very helpful, I think we all agree.  
20 The Maguire Institute has decided they are coming to  
21 Washington. They will take a full-time job and help us on  
22 this. We had quite a discussion last night. And I  
23 appreciate that. I am being a little bit facetious. But  
24 obviously, this is a subject that is on everyone's mind.

25 I was asked yesterday is the oil fee back on the

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1 table. Let me try to address that. The President said  
2 everything is back on the table. And I would say we have to  
3 take him at his word, that everything is back on the table.

4 That said, my personal opinion is that the oil  
5 import fee probably ranks pretty low on the list of things  
6 back on the table. And for this reason, the dislocation  
7 that has taken place in the securities industry, the banking  
8 community, severely hits the financial markets.

9 I don't know what you do with a country like  
10 Mexico that owes us \$100 billion. If you go back to the oil  
11 import fee, how do you put it back on imports from Mexico  
12 with the amount of money they owe our community? It looks  
13 counterproductive in that particular area.

14 We have just entered into a free trade agreement  
15 between the U.S. and Canada. The number one part of that  
16 agreement, and I would like to talk about it a minute, is  
17 the energy sector. Canada is our biggest supplier of  
18 imported oil today, and if you went back to import fee, I  
19 don't know what you would do with a situation with Canada.  
20 You certainly cannot go in the face of the free trade  
21 agreement with an import fee. It is specifically  
22 prohibited.

23 So if you knock out Canada and Mexico, I don't  
24 see the impact of the import fee. I think there are better  
25 places to look.

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1 So I am still not of a mind to encourage anyone  
2 that the oil import fee is a viable situation again.

3 I have looked at Bill Hogan's Harvard report  
4 which was put together. He shows a positive scenario for  
5 the oil import fee, but he makes the assumption that all the  
6 money you collect will go back directly into the economy,  
7 which is nonsense. It would be used for deficit reduction.  
8 I think that is living in another world, on a realistic  
9 basis.

10 So I will stand by the analysis that we have put  
11 in the energy security study that you saw come out in  
12 February. I will reference you to page 72, which is the oil  
13 import fee discussion if you have it to look at again. I  
14 believe that analysis is still pretty sound.

15 I think we have had some progress in stability of  
16 price. Price has been pretty stable between \$18 and \$20.  
17 My personal feeling from what I see is that that will  
18 continue.

19 People say, "Herrington, what about the fact that  
20 the oil embargo is going to force Iran to drive prices down  
21 and they will discount heavily, especially if Japan and  
22 other countries participate in the embargo?" I think that  
23 will give you a little bit of downward pressure. I can't  
24 help but think that after talking to King Fahd and the other  
25 leaders, leaders in Kuwait and President Zaid, that they

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1 will go to great lengths to defend the \$18 price and that  
2 will dominate the market.

3 What have we done inside the administration?  
4 Besides work on the tax credit, you saw the letter from the  
5 President last year. The administration may have had  
6 something to do with the rig count. We have worked hard on  
7 the windfall profits tax. I am encouraged by what I see. I  
8 think we have a general consensus that the windfall profits  
9 is a disaster; it is not a productive area for the  
10 administration on federal policy.

11 I am making a general statement because I think  
12 it took us a long time to get to that realization. I see  
13 people like Chairman Dingell, who now have recognized  
14 publicly and privately that the windfall profits tax is  
15 probably not a good idea.

16 There are problems. It is attached to the trade  
17 bill. The trade bill is a difficult bill. There is no  
18 question in my mind that if it stays in its present form,  
19 the President is going to have real difficulty signing it.  
20 But then again, we haven't seen the final form and we are  
21 still working to address the trade bill down to something we  
22 can live with. The trade bill today is a tremendously  
23 protectionist bill, and it will not help the economy of the  
24 U.S. It is attached to the reconciliation bill. I don't  
25 care what it is attached to, the windfall profits tax needs



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1 to go. It is a good signal, and we will keep working on  
2 that particular area.

3 We have worked very hard on the report from EPA  
4 to Congress from the Department of Energy, the Department  
5 of the Interior. It has been a joint effort on production  
6 waste. We have had a lot of help from API and a number of  
7 you in the industry, and I think we have made a lot of  
8 progress in this particular area. And I think that some of  
9 these unreasonable production regulations will be  
10 eliminated. And I am very pleased to see that.

11 We are making progress in resolving the ERA  
12 cases. We are settling more and more of those cases. We  
13 still plan to be able to abolish that particular program by  
14 the time we leave office. Hopefully, I will be there to  
15 turn out the lights.

16 Some of the cases are still difficult, but mainly  
17 we are getting good response from the industry, good  
18 reasonableness, and lawyers are working hard with us on our  
19 side and on their side, and we have reached some pretty  
20 reasonable settlements in that area.

21 ANWR, obviously, this is an area that has been  
22 very interesting to some of the majors. ANWR, I think,  
23 looks encouraging. I was encouraged last summer with the  
24 amount of people that got up to visit North Slope. I think  
25 we got key people up there. I liked the discussion. The

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1 Porcupine caribou issue seems to be going away. And we see  
2 efforts to bring in other issues, which means that maybe the  
3 Porcupine caribou issue is not the driving force this time.  
4 I would like to see us get away from that particular issue.

5 I would like to talk a second about the free  
6 trade agreement. I think this is on your mind. The free  
7 trade agreement is something that will be controversial in  
8 some areas. But from where I look at it, virtually all  
9 barriers to energy trade will be removed between the U.S.  
10 and Canada.

11 And I have been asked questions: are we going to  
12 affect FERC's authority through this particular free trade  
13 agreement? My answer is no. As-billed has been preserved.  
14 Current levels of trade are unaffected, and we don't have  
15 many barriers today. And this will prohibit us from  
16 erecting barriers.

17 I see this agreement as a model for the  
18 hemisphere. I think it is being underrated. If you really  
19 look at the implications of a free trade energy pact between  
20 the U.S. and Canada, it will make a lot of energy available  
21 at competitive prices. It is going to encourage the use of  
22 gas a lot, and I think that will be good for both sides. It  
23 is not going to affect programs to preserve and enhance  
24 reserve bases. If the U.S. Government wants to put  
25 incentives in for exploration and development, we can still

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1 do that and not be in violation of the agreement. And  
2 Canada can do likewise. So incentives are still there.

3 It is going to stop the dumping of cheap  
4 subsidized gas or any other kind of hydroelectric power on  
5 the U.S. market, and I think that is good for American  
6 producers. I would say that the free trade agreement is  
7 going to do a lot to stimulate gas production in the U.S.  
8 and in Canada and gas use.

9 The agreement, I think, from what we look at, if  
10 we could use it with more countries, it might come closer to  
11 establishing more of an interrelated energy market in this  
12 hemisphere.

13 So I like what I see on it, and I know a number  
14 of you are supportive, and some of you asked some questions.  
15 Let's see if I have finished before I open it up for  
16 questions here.

17 One other thing that I would like to mention is  
18 that we did receive from you the energy security report that  
19 was put together, called "Factors Affecting U.S. Oil and Gas  
20 Outlook." It came from EAB, Energy Advisory Board. We had  
21 the geoscience research energy security, and we have the  
22 advanced exploratory research report, Energy Council, oil,  
23 gas, shale, and we had the National Petroleum Council's  
24 report on factors affecting U.S. oil and gas outlook in the  
25 U.S.

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1 We had a lot of reports that have come through.  
2 We have a lot of information. And what are we doing about  
3 it?

4 One of the things I have done is I have created,  
5 along with Allen -- and I hope that you who have not gotten  
6 to know Allen Wampler and dealt with his department, know  
7 how receptive he has been to the industry and how much he  
8 has done in organizing the fossil area, especially in the  
9 oil and gas area. But together, Allen and I have created  
10 the office of geoscience research in his office of assistant  
11 secretary, which I think will do a lot towards bringing  
12 together research.

13 We have established a Department of Energy  
14 hydrocarbon geoscience research coordinating committee that  
15 will attempt to coordinate all of our geoscience research.

16 I sent a letter in July to the National Petroleum  
17 Council requesting you to address the petroleum research  
18 institute. It is a bit controversial. Some people have  
19 responded hat they don't want it because of the technology  
20 proprietary information traits. But what we ask you to do  
21 is to look at it to see if there is a place that we can help  
22 in working together with recovery technologies, if we can do  
23 anything to move together with the industry to help in the  
24 area of research and development and recovery.

25 C.J. Silas is proposed as chairman. He will have

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1 their first meeting November 8 in Chicago. Those of you who  
2 are asked to participate, I hope that you will have some  
3 input because I think it can be valuable if it is structured  
4 right.

5 Again, we are not looking for a federal solution  
6 to your problems. We are only looking to be helpful, to see  
7 if we can assist the industry and assist some of these  
8 programs and pull with you rather than at opposite ends.

9 I think that is about all I have to talk about in  
10 a general nature. I would be happy to try to take specific  
11 comments if they are necessary. But those are my general  
12 remarks. Thank you.

13 (Applause.)

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1 CHAIRMAN COX: Why don't we just open it up for  
2 questions and whoever would like to start off?

3 MR. GONZALES: This Administration inherited a  
4 very difficult energy situation because of the past mistakes  
5 made in energy policy. It is to be congratulated for the  
6 progress it has made, but as you recognized in your opening  
7 statements, we still have some things that need to be done.

8 The recent developments that emphasize the need  
9 for improvement in the national energy policies include the  
10 following:

11 The cost of U.S. Naval operations to protect  
12 shipments of oil in the Middle East.

13 The needed and long-term advantage to the nation  
14 of the 1986 energy price shock, the third in 14 years,  
15 caused by the action of oil exporting countries.

16 And the increasing costs of the Strategic  
17 Petroleum Reserve as it continues to be built up at the rate  
18 the Congress proposes.

19 In this situation we need to take some action to  
20 improve energy security which would be in accord with the  
21 sound principles, that appropriate fees should be levied to  
22 provide revenue to pay for what the federal government has  
23 to spend to deal with these problems.

24 Now, I agree with you that it would be nice if we  
25 could depend on a free market, but it is perfectly clear

FWbur 1 from the violent fluctuations in price that occurred between  
2 1985 and 1987, when there were very slight changes in the  
3 world demand and supply of petroleum, that the price of oil  
4 is subject to manipulation by exporting countries.

5 In that situation we have to ask ourselves what  
6 can be done to face up to the problem.

7 Now, in 1970, Secretary Schulz was the Chairman  
8 of the Cabinet Task Force on Oil Import Controls, in which  
9 the committee said:

10 "We recommend establishment of  
11 an absolute maximum for tariff-  
12 restricted Eastern Hemisphere oil  
13 imports equal to 10 percent of  
14 domestic demand."

15 It also recommended that should there be in  
16 excess of 10 percent of projected domestic demand from this  
17 area import licenses should be auctioned.

18 I agree with you that we should not impose a  
19 tariff on imports from Mexico and Canada or any place in the  
20 Western Hemisphere, but our problems have arisen from  
21 imports from the Eastern Hemisphere, a distant source, and  
22 because that is the cause of our need for a Strategic  
23 Petroleum Reserve, naval operations in the Persian Gulf, and  
24 so forth, it would be appropriate to levy a national  
25 security fee on oil imported from the Eastern Hemisphere

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1 only, including all products made from crude oil from that  
2 hemisphere.

3 A small fee of only 5 cents a gallon, which is  
4 \$2.10 a barrel, would have very little impact on the price,  
5 but it would signal the intention of the United States to  
6 recognize the cost, the hidden economic cost of depending on  
7 oil from distant sources.

8 And we could also announce that we would continue  
9 to exercise that fee until imports from that area dropped to  
10 the level indicated by the Cabinet, and this needs to be  
11 studied from an economic standpoint, and I hope that the  
12 Administration in the final period that it has will  
13 recognize what a great contribution could be made by taking  
14 some positive steps to show its concern about the risks  
15 involved in depending so heavily on oil imports from the  
16 Middle East.

17 SECRETARY HERRINGTON: You made some very good  
18 points, and I think those are the ones that we are wrestling  
19 with now.

20 I don't know if you accept my hypothesis that the  
21 dependence of the U.S. is not as heavy on the Middle East.  
22 I stated we only depend upon 3 to 5 percent. I think the  
23 main problem is the dependence of our allies on the Mideast  
24 and, in addition, the interlocking nature of our economies,  
25 and since we all know this is a world market, it is not a



P.Wbur

1 U.S.-Mideast market, the Strategic Petroleum Reserve I think  
2 has been a big factor -- it was mentioned in the Mideast  
3 when I was there a lot, and they want to know when we are  
4 going to use it.

5 How big it is. It is up to 535 million barrels  
6 today, and our policy is still firm to use it early on in an  
7 oil shock, and I think we are not backing off that  
8 particular policy, but I think you have made some good  
9 points.

10 I am not sure that there is a uniform agreement  
11 on that type of a fee, but I would be interested in a show  
12 of hands in this group. This is a group of very  
13 knowledgeable people, experts in the field, economists,  
14 lawyers, producers.

15 The type of fee that has been described obviously  
16 is a surcharge directed against one particular sector of the  
17 world market, and I would be interested for my own  
18 information how many in this room think that type of  
19 proposal would be a good thing.

20 Would you mind raising your hands?

21 (Show of hands.)

22 SECRETARY HERRINGTON: We get about four hands.  
23 How many think it would not be a good thing?

24 (Show of hands.)

25 SECRETARY HERRINGTON: We get a lot of hands.

Mr. Wbur

1 How many are undecided?

2 (Show of hands.)

3 SECRETARY HERRINGTON: We get a lot of hands on  
4 that.

5 And I think that is the problem. We are such an  
6 interrelated market today it is a very difficult particular  
7 area. The question that is hard for me to answer is why is  
8 the U.S. spending -- our costs today in the Gulf for the  
9 convoy is from 20- to \$30 million a month out of the Navy  
10 budget and risking American lives on ships where we are only  
11 importing 3 to 5 percent from that area. Why aren't our  
12 allies doing more? Why isn't Japan financing our whole  
13 convoy operation when they are taking one-third of the oil,  
14 and why do we have an oil embargo against Iran and Japan is  
15 still purchasing one-third of their oil from Iran? Aren't  
16 we working at cross purposes?

17 Those are very difficult questions that we have  
18 to get to in the next few months, and we have to insist on  
19 more support for our operations and more support for what we  
20 are doing in that particular area.

21 It is pretty obvious, I think, that this war  
22 needs to come to an end, and it needs to come to a peaceful  
23 solution or it must be confined out of the international  
24 waters. We simply cannot stand for the principle of  
25 allowing American flagships or even, in my estimation,

Mr. Wbur 1 American-owned ships, while they may not be American  
2 flagged, to be subjected to a belligerent nation that is  
3 traveling the sea lanes at will, machine gunning targets of  
4 opportunity.

5 Another question?

6 MR. CALDER: You express the opinion that the  
7 free trade bill with Canada would elicit greater production  
8 of gas.

9 Would you please give me the scenario of  
10 projected events that led you to come up with this opinion?

11 SECRETARY HERRINGTON: My opinions as a  
12 businessman/economist, I think gas would be more readily  
13 available and, since it is more available, it would be used  
14 as an energy source of choice more, and I think that as it  
15 is used more and more and would become -- using it more --  
16 you remember 1978 when Congressman Edward Markey wrote the  
17 New York Times? I was a businessman in California, and he  
18 said three things in his amazing editorial, and I remember  
19 reading it, never knowing I would be in the federal  
20 government or out of California. He said, number one:

21 Interest rates will never again -- the prime rate  
22 never again will drop below 20 percent, and he said  
23 inflation will never again be out of double digits and  
24 natural gas will never be a fuel of any significance in the  
25 United States.

FWbur

1 He said those three things in an editorial. I  
2 clipped it out and stuck it in my scrapbook and read it, and  
3 all three of those things were wrong.

4 So we are not very good at predicting. I think  
5 that point is loud and clear.

6 But when we went out and drilled for increased  
7 oil in the '70s after the '73 shock, the '79 shock, I think  
8 most of you will admit that we found a lot of natural gas.

9 The Fuel Use Act was one of the dumbest pieces of  
10 legislation to ever come along. I am very happy it is gone,  
11 and I hope that the industry appreciates what amount of work  
12 went into getting rid of this.

13 I think Frank mentioned last night that he thinks  
14 that the repeal of the Fuel Use Act has increased the use of  
15 gas. I don't know if I misheard you or not, Frank. That  
16 was basically a premise that it would help the use of more  
17 gas.

18 My own feeling is if we have a treaty in place  
19 between the U.S. and Canada that restricts cheap gas being  
20 dumped on the U.S. market in the future that it will level  
21 the playing field for U.S. industries and it would get more  
22 gas available. That is my general reasoning.

23 I would be interested to hear an opposite opinion  
24 if anybody has one.

25 MR. PITTS: The elimination of the Fuel Use Act I

Wbur 1 think has brought about something that could increase our  
2 use of natural gas, and we do need it because we have  
3 declined usage at the time from 22 trillion cubic feet down  
4 to 16 plus trillion.

5 The elimination -- and one of the reasons for the  
6 decrease was that we have not been selling the amount of gas  
7 to the electrical industry that we used to sell because of  
8 the declining volume. They are big users of natural gas.

9 I believe we can open up that market now, and I  
10 urge all of us, particularly the Energy Department as a  
11 leader, to help us condense the energy industry, the  
12 electrical industry, that the use of natural gas they should  
13 consider seriously and they are, but the -- two big  
14 questions, they tell me.

15 One is supply. They don't have confidence that  
16 we can have the reserves in the country to supply them if  
17 they invest in a plant.

18 And, secondly, will the spike come in price and  
19 force them not to use it?

20 They contend that they can use it up to \$4.50 per  
21 thousand cubic feet of gas. That gives us pretty good  
22 leeway up from what it is now.

23 I just offer that as a suggestion to our group.

24 SECRETARY HERRINGTON: I want to be as supportive  
25 as we can. We think gas is a very clean, efficient,

P.Wbur 1 environmentally safe fuel, and I want to be able to  
2 encourage as much gas use in the United States as I can and  
3 also the diversity of fuels. I hate to be hung up on coal  
4 or nuclear power, which is struggling now. If we can get  
5 gas back into the mix, I think it is the right thing to do.

6 Ed, I may be out of time.

7 CHAIRMAN COX: Are there other questions or  
8 comments?

9 VOICE: You talked about your conversations with  
10 the Saudis and the continuing reluctance to give them  
11 weapons.

12 Has this affected our relations any?

13 SECRETARY HERRINGTON: It is hard to be on a  
14 confidential basis with half of the Washington press sitting  
15 out there.

16 (Laughter.)

17 I love these guys.

18 On an unconfidential basis, they are disappointed  
19 -- there is no question -- on our inability to provide them  
20 sufficient arms sales to allow them to defend themselves,  
21 and I think with good cause. I think we have an obligation  
22 to make these weapons sales, and I think too much politics  
23 has entered into it. But there is no question that they are  
24 frustrated.

25 A number of the leaders -- I will not mention by

Mr. Wbur 1 name because it would be in the paper tomorrow -- they sat  
2 there and read me comments from the Washington Post and  
3 other American papers, New York Times, and said, why is this  
4 senator saying that about us?

5 They don't understand our process and the fact  
6 that we are now conducting most of our business in public,  
7 and I think that is too bad.

8 MR. PARKER: Since the press is here, we should  
9 keep a perspective, and I know that you identified it, but  
10 our dependency on the Middle East oil is much larger. Our  
11 allies have a call, and if we are cut off and we do not have  
12 a call and we lose much of the other supplies scrambling for  
13 the market, I know you are aware of that, but sometimes --  
14 we really would miss it if we were cut off. There are too  
15 many other people. The allocation that we have worked out  
16 in the world today leaves us depending on a very small  
17 amount but with the loss of that source of supply it would  
18 be a major problem for all of us.

19 SECRETARY HERRINGTON: I couldn't agree more.

20 Let me mention if I could for a second, there are  
21 two things that struck me during this trip that I think are  
22 significant. A number of you are well aware of this,  
23 especially in light of the amount of pipeline construction  
24 that is going on from Iraq through Turkey, from Iraq through  
25 Saudi Arabia into Dubai and out through the different

Wbur 1 sources. It is easy to write a scenario today that will see  
2 in the early '90s up to 7 million barrels a day moving by  
3 pipeline out of the Gulf, which is a fairly secure source.

4 I think there is a substantial movement away from  
5 the Strait of Hormuz bottleneck that we see, and I think that  
6 is significant, a political change in what we have seen over  
7 there heretofore. That is number one.

8 Number two, most of you know about this and some  
9 of you don't, we were briefed in Cuddeback about the size of  
10 the North Dome gas field, the biggest gas field in the world  
11 -- and it truly is monumental -- if that gas can get to  
12 market it is going to be a substantial change in the LNG  
13 market, in the gas market.

14 Those of you involved and are interested, I would  
15 urge you to get briefed up on the size, the location, and  
16 the ramifications of that particular field. They hope to  
17 bring it on within two or three years. It is one of the  
18 biggest -- in fact the biggest reserve I have ever seen, and  
19 I am sure it is the biggest reserve we have ever heard of.

20 That is it, Ed. Thank you very much.

21 (Applause.)

22 CHAIRMAN COX: Thank you, Mr. Secretary. We are  
23 indebted to you for being here. We are looking forward to  
24 the current projects that we have underway and continuing  
25 them and others that you may request from time to time.



P.Wbur

1 As the Secretary noted, he did request the  
2 industry's perspective on how to promote research and  
3 development to increase recovery of petroleum already  
4 discovered and develop longer range technologies.

5 To this end, the request calls for the Council to  
6 examine the advisability and feasibility of establishing the  
7 Petroleum Research Institute. A copy of the Secretary's  
8 letter is among the handouts this morning.

9 Because of the urgency that the Secretary  
10 attached to this subject, I exercise the right to -- granted  
11 under Section 7-1 of the Articles of Organization -- to  
12 proceed with the establishment of a committee to begin  
13 preparing a response. With the Secretary's approval, I  
14 would form the Committee on the Reserve Institute.

15 Pete Silas of Phillips has agreed to be the  
16 Chairman. The full committee roster has been submitted to  
17 the Secretary for his formal approval, and a copy of that  
18 roster is also in your folder.

19 The committee is going to begin immediately, and  
20 we will have a report from the committee at our next  
21 meeting, at which time there will be a full discussion of  
22 the results and conclusions that they reach at that time.

23 So if there are any questions, we will entertain  
24 them at that point.

25 We also want a report from Bill Swales, if he

P.Wbur

1 will. As you know, he has acted as Chairman of the  
2 Petroleum Storage and Transportation, requested by the  
3 Secretary at our last meeting, and so he will give us a  
4 status report and the schedule for its completion.

5 Bill.

6 MR. SWALES: Thank you, Mr. Chairman, ladies and  
7 gentlemen.

8 I am pleased to present you this morning a status  
9 report on the Petroleum Storage and Transportation Study.  
10 As you may recall at our last meeting, we agreed to the  
11 Secretary of Energy's request that the National Petroleum  
12 Council undertake a comprehensive study updating the  
13 Council's petroleum inventory, storage, and transportation  
14 capacity reports of 1979 and 1984.

15 The Secretary requested -- and I quote from his  
16 letter:

17 "Emphasis should be given to  
18 the reexamination of minimum  
19 operating inventory levels,  
20 the location of storage  
21 facilities and availability of  
22 inventories in relationship to  
23 local demand and the capabilities  
24 of distribution networks to move  
25 products from refining centers

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1 to their point of consumption,  
2 particularly during periods of  
3 stress."

4 The Secretary's complete request letter is  
5 appended to the study paper in your packets this morning.

6 The last time the Council issued a report on all  
7 of these areas -- inventory, storage, and transportation  
8 capacities -- was in 1979. The inventory and storage  
9 capacity portions of that study were updated in the NPC's  
10 1984 report for the Secretary, entitled "Petroleum  
11 Inventories and Storage Capacity."

12 The 1984 report was the tenth report since 1948  
13 prepared by the NPC. The objectives have evolved over time.

14 The principle objective of the early studies was  
15 to determine the total storage capacity of the primary  
16 distribution system and the amount of petroleum inventory  
17 that could physically be delivered from the system in the  
18 even of a military emergency.

19 In 1974, the Council began focusing on  
20 inventories that might be available during nonmilitary  
21 emergencies by estimating minimum operating inventories.  
22 These minimums, which are significantly higher than the  
23 physical minimums, are defined as level of petroleum stocks  
24 in primary inventories below which operating problems and  
25 spot shortages would begin to appear.

P.Wbur 1 In 1979, the Council added estimates of inventory  
2 and storage capacities in the secondary sector and in '84  
3 included estimates of inventories and storage in the  
4 consumer, or tertiary sector.

5 In his request letter, the Secretary noted that  
6 the 1979 and '84 reports are the most current comprehensive  
7 treatment of this subject available, although some of the  
8 data are now nearly a decade old. The minimum operating  
9 inventory levels for resids based on the '83 data are no  
10 longer considered valid by the Department of Energy and  
11 therefore are no longer referenced in the Energy Information  
12 Administration publications.

13 The petroleum transportation data were compiled  
14 in 1978, and as we all know, there have been a number of  
15 changes since then in the way the industry transports and  
16 distributes crude oil, petroleum products, and natural gas.

17 To undertake this study, the Council established  
18 the Committee on Petroleum Storage and Transportation. I am  
19 honored to have Dr. Helmut Merklein, Administrator, Energy  
20 Information Administration, as my government Co-Chairman.

21 Our committee met on September the 30th, 1987,  
22 and as one of its first acts established a coordinating  
23 subcommittee under the direction of Riad Yammine of  
24 Marathon. It will aid in directing the overall study effort  
25 and has three task groups -- Liquid Transportation Task

P.Wbur 1 Force, chaired by John P. DesBarres, President of Sun  
2 Pipeline; the Transportation Task Force chaired by Ronald J.  
3 Burns, Executive Vice President, Enron Gas; the Inventory  
4 and Storage Task Force, chaired by Bruce V. Frolick, Vice  
5 President - Supply and Distribution, Chevron USA, Inc.

6 Each of these groups have a broad membership  
7 which includes representatives of both major and independent  
8 petroleum companies, natural gas producers and pipelines,  
9 the electric power industry, energy research associations,  
10 and academia and consulting committees.

11 Rosters of these study groups are also attached  
12 to the study paper in front of you.

13 The committee, with the assistance of these  
14 groups, will determine physical changes that have occurred  
15 in petroleum and gas transportation systems since the 1979  
16 report, emphasizing pipeline and water borne transportation.

17 It is believed that the other transportation  
18 modes, tank cars, tank trucks, do not require separate task  
19 groups as in the past and that accurate information may be  
20 available from corporations in studies from other sources.

21 The committee will also update the petroleum  
22 inventory and storage data from the 1984 report, including  
23 new minimum operating inventory levels for crude oil and the  
24 principal petroleum products and estimates for storage  
25 capacity and inventory levels in the secondary and consumer

P.Wbur

1 sectors.

2 Natural gas storage will also be studied as part  
3 of the gas transportation group effort.

4 It is expected that most of these data will be  
5 collected by survey. The data from these efforts will be  
6 examined to determine stress points in the system caused by  
7 possible shifts in both supply and demand in the next five  
8 years.

9 The Strategic Petroleum Reserve will also be  
10 examined as a source of emergency supply, relying heavily on  
11 the Council's 1984 report of the Strategic Petroleum  
12 Reserve.

13 In addition to these analyses, we will examine  
14 changes in the petroleum market due to the various factors,  
15 including the expansion of the futures market, changes in  
16 the natural gas industry brought about by the regulatory  
17 policies changes implemented through the recent FERC orders  
18 that move toward a more open marketplace.

19 The study will also examine the impact of changes  
20 in pipeline safety requirements, environmental and other  
21 regulations.

22 Finally, we intend to place much greater emphasis  
23 on the dynamics and interrelationship of the petroleum and  
24 natural gas supply systems, including the role of changing  
25 supply sources, fuel switching, and cogeneration.

P.Wbur

1                   At this time I would like to ask for your  
2 assistance with the surveys that many of you will be  
3 receiving in the spring from the committee. These surveys  
4 are essential to the study and, as members of the National  
5 Petroleum Council, you have an excellent record of  
6 responding to the surveys for past studies.

7                   What I am asking is that you see to it that they  
8 are filled out and returned promptly.

9                   The committee has set an ambitious timetable for  
10 this study that would result in a final report for your  
11 consideration by next winter. The coordinating subcommittee  
12 and the task groups will be required to meet frequently over  
13 the next year in order to meet the schedule, and I look  
14 forward to presenting to you the progress report at our  
15 spring meeting and a final report at the winter meeting.

16                  Mr. Chairman, that concludes my remarks. Are  
17 there any questions?

18                  CHAIRMAN COX: Are there any questions of Bill?

19                  (No response.)

20                  CHAIRMAN COX: Thank you very much, and we will  
21 be looking forward to getting your other report in the  
22 spring. At that time we will also hopefully have our  
23 Petroleum Research Study underway and results by then.

24                  We had hoped -- up until I received a call last  
25 night -- that Jim Miller of OMB was going to -- hopefully he

Mr. Wbur 1 was going to be with us today, but unfortunately he called  
2 last night during the reception and said because of the  
3 pressures on the budget and problems that the Administration  
4 is working on right now with Congress that he would not be  
5 able to be here. He did express hope that he would be able  
6 to be here with us at our next meeting.

7 So we are sorry that we do not have an  
8 opportunity to hear from him today, especially in view of  
9 everything that is happening today.

10 We would like to call right now on John Hall.  
11 John is Chairman of the Finance Committee, and it is people  
12 like John, Bill, and all of the others who work on these  
13 various task forces and chair these various efforts that  
14 make this Council work.

15 So we are indebted to you, John, and to everyone  
16 else for the hours that you spend. Your time is even more  
17 important, and it is a pleasure to call on John, who will  
18 report from the Finance Committee that met yesterday  
19 afternoon.

20 MR. HALL: Mr. Chairman, members of the Council.

21 The Finance Committee met yesterday to review the  
22 financial status of the Council. We reviewed a draft of the  
23 calendar year 1986 audit report from the Council's  
24 independent outside auditor, who is Arthur Young and  
25 Company, as well as we reviewed expenditures for the first



P.Wbur

1 nine months of the calendar year.

2 I am pleased to report the financial position of  
3 the Council is sound. We are in certificates of deposit,  
4 with surplus money.

5 (Laughter.)

6 In fact, we expect to end 1987 with a sizable  
7 surplus. The surplus is a result of cost cutting and the  
8 fact that the majority of the cost of the Petroleum Storage  
9 and Transportation Study will be incurred in 1988 instead of  
10 late 1987, as budgeted.

11 We then discussed calendar year 1988 and a  
12 recommended budget in the amount of \$1,750,000. This budget  
13 includes the funds to complete the Petroleum Storage and  
14 Transportation Study and the Petroleum Research Study that  
15 we discussed earlier.

16 Even though this budget is a slight increase over  
17 1987, it is 17 percent lower than three years ago.

18 The recommendation for member contributions to  
19 support the budget will be made at our spring meeting.  
20 However, at this time it appears that contributions at the  
21 current level will be satisfactory.

22 Finally, the Finance Committee recommends that  
23 Arthur Young and Company continue as our independent public  
24 accountants for examination of our 1987 financial  
25 statements.

P. Wbur

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Thank you, Mr. Chairman, and I move that the report of the Finance Committee be approved by the Council.

MR. SWALES: Second.

CHAIRMAN COX: I believe there are two motions, approval of the report and also the approval of Arthur Young as auditors.

All in favor of both of them, say "aye."

(Chorus of ayes.)

CHAIRMAN COX: Opposed?

(No response.)

CHAIRMAN COX: We are not supposed to do it that way, but that worked out, I think.

(Laughter.)

CHAIRMAN COX: We referred several times to the spring meeting, and the date has been set, with concurrence of the Secretary, of April 21st. We will have the reception the evening before on the 20th, and you will get further confirmation of that, but so that you can make your calendar dates now we want you to be aware of this.

This brings us to the end of our formal agenda this morning, and next time we hope to have two additional speakers for you in addition to the Secretary, and we are sorry that Director Jim Miller could not be here with us this morning.

We would like to open the meeting for any other

1 matters or any further discussions that anyone might like to  
2 bring at this time.

3 We will limit this not only to members -- we will  
4 not limit it just to members of the Council but any of our  
5 guests who have -- any non-Council members who would like to  
6 make a remark. We would like to hear from them.

7 Are there any comments or questions?

8 (No response.)

9 CHAIRMAN COX: We thank you very much for being  
10 here.

11 There being no further business, we will stand  
12 adjourned.)

13 (Whereupon, at 10:06 a.m., the meeting was  
14 adjourned.)

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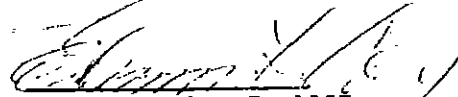
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THE NATIONAL PETROLEUM COUNCIL

I hereby certify that this transcript constitutes an accurate record of the meeting of the National Petroleum Council held on October 28, 1987.

Edwin L. Cox  
Chairman



Date: December 7, 1987